

Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 IO-13 ISO-00 AID-05 CIAE-00 COME-00

EB-07 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02

OPIC-03 SP-02 CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05

SS-15 STR-04 CEA-01 DODE-00 PM-04 H-02 L-03 PA-01

PRS-01 EURE-00 /111 W

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P R 241822Z NOV 76

FM AMEMBASSY BONN

TO SECSTATE WASHDC PRIORITY 3560

INFO AMEMBASSY LONDON

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY TOKYO

USMISSION EC BRUSSELS

USMISSION OECD PARIS

USMISSION USBERLIN

USMISSION NATO BRUSSELS

USDEL MTN GENEVA

USNMR SHAPE

AMCONSUL FRANKFURT

AMCONSUL MUNICH

AMCONSUL BREMEN

AMCONSUL DUSSELDORF

AMCONSUL HAMBURG

AMCONSUL STUTTGART

CINC USAFE RAMSTEIN

CINC USAREUR HEIDELBERG

CINC EUR VAIHINGEN

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DEPARTMENT PASS TREASURY, FRB AND CEA

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E.O. 11652: N/A

TAGS: EFIN, ECON, GW

SUBJECT: FRG COUNCIL OF ECONOMIC ADVISORS' REPORT
SUGGESTS STIMULATION PROGRAM

1. THE FRG COUNCIL OF ECONOMIC ADVISORS ("FIVE WISE MEN") ISSUED THEIR ANNUAL ECONOMIC REPORT NOVEMBER 24 IN A SOMEWHAT DIFFERENT FORM THAN USUAL. THIS TIME, TWO FORECASTS FOR THE COMING YEAR WERE PRESENTED. ONE, LABELED "STATUS QUO" AND REFLECTING A CONTINUATION OF PRESENT POLICIES, LED TO 4.5 PERCENT REAL GNP GROWTH--A FULL PERCENTAGE POINT BELOW WHAT THE GOVERNMENT AND ECONOMIC RESEARCH INSTITUTES HAD EARLIER BEEN FORECASTING. THE SECOND FORECAST OF 5 TO 5 1/2 PERCENT GROWTH INCORPORATED IN THE COUNCIL'S REPORT WAS BASED ON THE ASSUMPTION THAT CERTAIN EXPANSIONARY MEASURES COSTING ABOUT DM 3 BILLION WOULD BE UNDERTAKEN BY THE GOVERNMENT. THE STRONG IMPLICATION IS THAT THE COUNCIL RECOMMENDS THE ADOPTION OF THE PROGRAM. ALTHOUGH IT IS STILL TOO EARLY TO REPORT REACTIONS TO THIS APPROACH (WHICH WE WILL DO LATER, ALONG WITH PROVIDING FURTHER ANALYSIS), IT SEEMS THAT THE GOVERNMENT WOULD BE HARD PUT TO IGNORE THE QUASI-INDEPENDENT BUT PRESTIGIOUS COUNCIL'S RECOMMENDATION.

2. THE COUNCIL OF ECONOMIC ADVISORS MADE SOME CONCRETE SUGGESTIONS FOR CHANGES IN ECONOMIC POLICY, THEY SAID, TO REDUCE DOWNSIDE RISKS OF MAINTAINING THE CURRENT COURSE AND TO MAKE POSSIBLE A HIGHER RATE OF GROWTH. IT ALSO IS INTENDED TO REDUCE DEPENDENCE ON FOREIGN TRADE. THE PACKAGE OF MEASURES COSTING APPROXIMATELY DM 3 BILLION CONSISTS OF THE FOLLOWING:

(A) CHANGES IN BUSINESS TAX REGULATIONS WHICH WOULD PERMIT MORE RAPID AND LIBERAL DEPRECIATION ALLOWANCES,

(B) STRENGTHENING OF RESEARCH AND DEVELOPMENT EFFORTS, PARTICULARLY WITHIN THE SMALL AND MID-SIZED LIMITED OFFICIAL USE

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FIRMS,

(C) THE ESTABLISHMENT OF A CREDIT-SUBSIDY SCHEME TO FACILITATE THE ESTABLISHMENT OF NEW FIRMS, AND

(D) PROVIDE FOR AN ADDITIONAL GOVERNMENT-FINANCED LABOR MARKET PROGRAM TO FACILITATE REGIONAL AND VOCATIONAL MOBILITY OF WORKERS.

3. THE FINANCING OF THIS DM 3 BILLION PROGRAM IS SEEN BY THE COUNCIL AS STEMMING MAINLY FROM A ONE POINT INCREASE (FROM 11 TO 12 PERCENT) IN THE VALUE ADDED TAX (VAT) EFFECTIVE JULY 1, 1977. THIS MEASURE WOULD RAISE DM 2 1/2 BILLION; THE REMAINING HALF BILLION FINANCING THE COUNCIL SUGGESTS COULD COME FROM SAVINGS MADE IN OTHER BUDGETARY CATEGORIES.

4. THE PROGRAM SHOULD BE SUPPORTED BY THE FOLLOWING ADDITIONAL POLICY MEASURES:

(A) FISCAL POLICY SHOULD PROVIDE FOR A 5 PERCENT INCREASE IN THE BUDGETS OF THE PUBLIC SECTOR.

(B) THE MONETARY POLICY SHOULD BE ONE THAT WOULD BE GUIDED BY A 6 1/2 PERCENT GROWTH GOAL IN CENTRAL BANK MONEY; IN THE CASE OF AN INCREASE IN VAT,

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SS-15 STR-04 CEA-01 DODE-00 PM-04 H-02 L-03 PA-01

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P R 241822Z NOV 76

FM AMEMBASSY BONN

TO SECSTATE WASHDC PRIORITY 3561

INFO AMEMBASSY LONDON

AMEMBASSY PARIS

AMEMBASSY ROME

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USMISSION EC BRUSSELS

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IT SHOULD BE RAISED TO 7 PERCENT.

(C) THERE SHOULD BE A MAINTENANCE OF A FLEXIBLE
EXCHANGE RATE POLICY WITH CURRENCIES OUTSIDE THE
SNAKE.

(D) A PART OF WAGE INCREASES SHOULD BE RELATED
TO PROFITS AND PAID OUT IN SOME FORM OF STOCK
PARTICIPATION IN THE EMPLOYING FIRM.

5. THE COUNCIL EMPHASIZES THAT THIS PROGRAM IS AIMED
AT MEDIUM-TERM STRUCTURAL CHANGES RATHER THAN A
QUICK SHOT IN THE ARM TO STIMULATE THE ECONOMY
ON A SHORT-TERM AND TEMPORARY BASIS. HOWEVER, THEY DO
SAY THAT IF THE PROGRAM IS IMPLEMENTED, THE EFFECTS
WOULD BE FELT NEXT YEAR IN RESPECT TO PRODUCTION,
EMPLOYMENT AND INCOME. IN ORDER TO CLARIFY THIS, THE
COUNCIL SPECIFIES, IT INCLUDED TWO FORECASTS. ONE
WITHOUT INCORPORATION OF THE RECOMMENDED MEASURES,
"THE STATUS QUO", AND ANOTHER BASED ON THE ASSUMPTION
BASIS THAT THEIR RECOMMENDED MEASURES ARE IMPLEMENTED
IN THEIR ENTIRETY. THE TABLE WHICH DETAILS THESE
TWO FORECASTS FOLLOWS:

COUNCIL FORECASTS FOR 1977
(PERCENT CHANGE UNLESS OTHERWISE STATED)

FORECAST WITH
"STATUS QUO" STIMULATION

	FORECAST	PROGRAM
CHANGE IN GNP (1962 PRICES)		
PRIVATE CONSUMPTION	5	4 1/2
PUBLIC CONSUMPTION	2 1/2	2 1/2
GROSS FIXED INVESTMENT	5	7
MACH. & EQUIP.	7 1/2	10 1/2
BUILDINGS	2	2 1/2
EXPORTS	9	8 1/2
IMPORTS	9	9 1/2
GNP	4 1/2	5 TO 5 1/2
UNEMPLOYMENT	900,000	800,000
PRIVATE CONSUMPTION DEFLATOR	4	4 TO 4 1/2(A)
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GNP DEFLATOR	4	4
DISPOSABLE INCOME	8 1/2	8
NET INCOME		
EMPLOYEES	7 1/2	8
BUSINESS	10 1/2	12

(A) THE HIGHER DEFLATOR IF THE VAT IS INCREASED ONE
PERCENTAGE POINT JULY 1, 1977.

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